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Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

CORDIS CORPORATION,

Petitioner,

vs.

MEDTRONIC, INC.,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

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QUESTIONS PRESENTED

1. Is the public interest served by allowing the Federal Circuit to subvert federal patent policies in favor of contract principles, contrary to this Court's mandate in its landmark decision in *Lear v. Adkins* and, more specifically, by precluding a patent licensee from escrowing royalties during his challenge of an invalid patent?

2. Are the interests of the U.S. patent system served by the Federal Circuit when it denies a patent licensee the right to escrow royalties during his challenge of an invalid patent, contrary to the decision of this Court (and the Sixth and Seventh Circuits) which held that a licensee should *not* be compelled to pay royalties while challenging the validity of the licensed patent?

PARTIES TO THE PROCEEDING

The parties to the proceeding below are CORDIS CORPORATION, plaintiff in the District Court and appellee in the Court of Appeals, and MEDTRONIC, INC., defendant in the District Court and appellant in the Court of Appeals.[1]

[1] Pursuant to Rule 28.1 CORDIS CORPORATION has no parent company or wholly owned subsidiary. It is affiliated with Cordis-Dow, of Midland, Michigan.

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CORDIS CORPORATION,

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vs.

MEDTRONIC, INC.,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

CORDIS CORPORATION (hereinafter CORDIS), hereby petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Federal Circuit. This Petition is occasioned by the Court of Appeals' failure to apply the federal patent policy mandate of *Lear, Inc. v. Adkins*, 395 U.S. 653 (1969).

OPINIONS BELOW

The Court of Appeals' Opinion of December 17, 1985, vacating the District Court's Order, is reported at 780 F.2d 991, and is included at pages 1a-8a in the Appendix to this Petition. CORDIS' Petition For Rehearing was denied, without opinion, on February 14, 1986 (9a).

The District Court's Order of January 9, 1985, granting CORDIS' Motion For Establishment of Escrow Fund and For Preliminary Injunction, is reported at 606 F. Supp. 132 and is included in the Appendix at pages 10a-12a.

GROUNDS OF JURISDICTION

The opinion of the Court of Appeals for the Federal Circuit was entered on December 17, 1985, and a timely-filed Petition For Rehearing was denied on February 14, 1986.

This Court has jurisdiction under 28 U.S.C. 1254(1).

CONSTITUTIONAL PROVISIONS INVOLVED

CONSTITUTION:

Art. 1, Sec. 8, Cl. 8

> The Congress shall have power... To promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries.

Art. VI, Cl. 2

> This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby; any Thing in the Constitution or Laws of any State to the Contrary nothwithstanding.

STATEMENT OF THE CASE

1. The Factual Background And The Decision Below

CORDIS is non-exclusively licensed by MEDTRONIC, INC. (hereinafter "MEDTRONIC"), under two United States patents (i.e., the licensed patents in suit). In September, 1984 CORDIS became aware of important "new evidence" pertaining to the validity of the licensed patents. As acknowledged by the Court of Appeals, this evidence was arguably sufficient to establish the invalidity of the licensed patents (8a).

In October, 1984, CORDIS requested that MEDTRONIC agree to a voluntary escrow of royalties accruing under the License Agreement until the new evidence was heard and evaluated in a case then pending in the District of Minnesota. MEDTRONIC refused.

Accordingly, on October 19, 1984, CORDIS filed a Complaint for Declaratory Judgment of invalidity of the licensed patents in suit,[2] and simultaneously moved: (1) to establish an interest bearing escrow account for the receipt of royalty payments due and owing to MEDTRONIC under the terms of the License Agreement during the pendency of this Declaratory Judgment action, the funds accumulated in the escrow account to be disbursed to the prevailing party in this action; and (2) to enjoin MEDTRONIC from terminating the License Agreement during the pendency of this Declaratory Judgment action.

The Motion was fully briefed by both parties, and oral argument was held. On January 9, 1985 the District Court granted CORDIS' Motion and established the proposed escrow and injunction. The District Court concluded that:

> [t]he circuits are split on the issue of whether to establish escrow accounts for the collection of royalty payments during the pendency of patent infringement suits. I have

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[2] The District Court has original and exclusive jurisdiction of this cause of action under 28 U.S.C. 1338.

decided, however, that *Precision Shooting Equipment Co. v. Allen*, 646 F.2d 313 (7th Cir. 1981) and *Atlas Chemical Industries, Inc. v. Moraine Products*, 509 F.2d 1 (6th Cir. 1974) are more faithful to the spirit of *Lear, Inc. v. Adkins*, 395 U.S. 653 (1969), where the Supreme Court held that licensee estoppel is no longer valid law."[3]

MEDTRONIC appealed the entry of that Order.

2. The Federal Circuit's Decision

On December 17, 1985, the Court of Appeals for the Federal Circuit vacated the District Court's Order and remanded this case to the District Court for further consideration. The Court concluded that the District Court made several errors of law relating to the interpretation and application of *Lear, Inc. v. Adkins*, 395 U.S. 653 (1969).

According to the Court of Appeals, the District Court misapplied *Lear* in evaluating the rights and obligations of the parties and the interest of the public (6a). In particular, the Federal Circuit decided that the District Court erred "in ruling that the *Lear* decision is implicit authority for permitting a licensee to deposit royalties due *pendente lite* into an escrow account pending a determination on the merits" (4a). The Court of Appeals could "find no authority in *Lear* for establishing an escrow for royalties due *pendente lite* or preliminarily enjoining a licensor from cancelling the license agreement" (5a), and held that *Lear* only precluded "the affirmative enforcement by the licensor of the royalty payment provision of the license agreement while the patent's validity is being challenged by the licensee" (6a).

The Court of Appeals also found that the District Court erred, with respect to the requirement of irreparable harm, in

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[3] The contrary circuit court decisions are *Warner-Jenkinson Co. v. Allied Chemical Corp.*, 567 F.2d 184, 193 USPQ 753 (2d Cir. 1977); and *Nebraska Engineering Corp. v. Shivvers*, 557 F.2d 1257, 195 USPQ 227 (8th Cir. 1977).

"reading that the Sixth Circuit *Troxel* (I)[4] opinion is authority for the proposition that a licensee may never recoup royalties" (4a-5a). Although holding that the District Court's reliance on Troxel (I) was faulty, the Court of Appeals *specifically declined* to decide whether a licensee who is successful in its validity challenge is entitled to the return of royalties paid *pendente lite* (8a).

REASONS FOR GRANTING THE WRIT

I. THE COURT OF APPEALS' DECISION IS CONTRARY, IN RATIONALE AND EFFECT, TO THE SUPREME COURT'S MANDATE IN *LEAR*

Lear v. Adkins, 395 U.S. 653 (1969), is a watershed decision in patent law. Reversing over a century of case law, *Lear* abolished the doctrine of licensee estoppel (which precluded a patent licensee from challenging the validity of the licensed patent) and held that a licensee may not be compelled to pay royalties while challenging the validity of the licensed patents. Indeed, *Lear* established, once and for all, the preeminence of federal patent policy over contract doctrine.

In abolishing licensee estoppel, the Court stated:

> Surely the equities of the licensor do not weigh very heavily when they are balanced against the important public interest in permitting full and free competition in the use of ideas which are in reality a part of the public domain. *Licensees may often be the only individuals with enough economic incentive to challenge the patentability of an inventor's discovery. If they are muzzled, the public may continually be required to pay tribute to would be monopolists without need or justification.* (Emphasis added)

395 U.S. at 670.

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[4] *Troxel Mfg. Co. v. Schwinn Bicycle Co.*, 465 F.2d 1253, 175 USPQ 65 (6th Cir. 1972).

Similar reasoning also supported the holding that a licensee may not be required to pay royalties while challenging patent validity:

> The parties' contract, however, is no more controlling on this issue than is the State's doctrine of estoppel, which is rooted in contract principles. *The decisive question is whether overriding federal policies would be significantly frustrated if licensees could be required to continue to pay royalties during the time they are challenging validity in the courts.*
>
> *It seems to us that such a requirement would be inconsistent with the aims of federal patent policy.* Enforcing this contractual provision would give the licensor an additional economic incentive to devise every conceivable dilatory tactic in an effort to postpone the day of final judicial reckoning. We can perceive no reason to encourage dilatory court tactics in this way. Moreover, the cost of prosecuting slow-moving trial proceedings and defending an inevitable appeal might well deter many licensees from attempting to prove patent invalidity in the Courts. (Emphasis added)

395 U.S. at 673.

This language is plain and unequivocal. It sets forth a public policy mandate based on the pre-eminence of federal patent policy over private contract doctrine, which is not and should not be limited to the particular facts in *Lear*. The Supreme Court repeatedly emphasized in *Lear* that to implement this mandate: (1) the licensee, who may be the only person with sufficient interest to challenge patents believed to be invalid, must be unmuzzled; (2) obstacles which may chill or frustrate a licensee's willingness to undertake a validity challenge or which may give rise to dilatory tactics or delay by the licensor must be removed; and (3) prompt and vigorous resolution of patent validity issues must be encouraged.

If not reversed, the Federal Circuit's refusal to allow post-challenge royalties to be deposited into an escrow account, without threat of license termination, will undo the very thing *Lear* sought to accomplish. In stark contrast to the public

policy objectives of *Lear*, the Federal Circuit's decision places substantial obstacles in the path of a patent licensee who seeks to challenge patent validity; creates real incentives for delay and for dilatory court tactics; and, in the end, muzzles the licensee as effectively as if the *Lear* decision never existed. The Federal Circuit decision would allow patent licensors to avoid the consequences of *Lear* by the simple expedient of terminating the license if the licensee refuses to pay royalties to the licensor during the validity challenge. In such event, the licensee would, of course, be exposed to the threat of an injunction, treble damages and other relief — a result which *Lear* specifically sought to avoid.

As *Lear* is interpreted by the Federal Circuit, a patent licensee who believes the licensed patent(s) to be invalid (even if based on information discovered after entering the license) has only two courses of action: (1) continue to pay royalties to the licensor (thereby funding the licensor's war chest) while litigating validity, without any assurance of the return of the royalties if successful, or (2) cease paying royalties, thereby automatically exposing itself to license termination, and potential injunction, treble damages and other relief.

This is truly a "Hobson's choice" which frustrates the overriding federal policies of *Lear* just as surely as actually ordering that royalties be paid during the litigation. In the first alternative, the licensee must pay the royalties accruing *pendente lite* without any assurance of their return. Although the Federal Circuit decision held that *Troxel* (I) did not preclude return of royalties paid *pendente lite*, the *Court expressly refused to decide whether such royalties should be returned.* Thus, the issue of entitlement to royalties paid *pendente lite*, remains in substantial doubt, steeped with uncertainty. Certainly, based on this authority, counsel could not advise a client that post-challenge royalties would definitely be refunded if the challenge is successful.

The practical result is, of course, that it is highly unlikely that a licensee would be willing to undertake the time, expense,

and other risks associated with a patent validity challenge, if the licensee were required to continue paying royalties that *may* not be refundable. Should a licensee choose to proceed with such litigation, and is found not to be entitled to recover post-challenge royalties, the licensor will have achieved indirectly that which *Lear* directly prohibited — i.e., requiring the payment of royalties during a validity challenge (395 U.S. at 673).

The second alternative offers the same unacceptable risks to a licensee. By refusing to pay royalties during litigation, the licensee is exposed to likely termination of the license and thus to an injunction, increased damages, and other relief. CORDIS respectfully submits that most reasonable and well-advised licensees would not pursue this undesirable choice.

Accordingly, the practical effect of the Federal Circuit's decision is the very result which the Supreme Court sought to avoid in *Lear*. Licensed patents believed to be invalid simply will not be litigated, and the licensor will continue to profit to the detriment of the licensee and to the public.

II. THE OVERRIDING PUBLIC POLICY ARTICULATED IN *LEAR* AND THE INTERESTS OF BOTH PARTIES AND THE PUBLIC ARE BEST SERVED BY ESCROWING ROYALTIES ACCRUING *PENDENTE LITE*

The interesting-bearing escrow established by the District Court is an even-handed and responsible way of implementing the public policy considerations of *Lear* and maintaining the status quo — without unduly interfering with the contractual arrangements between the parties. More particularly, the escrow permitted by the District Court protects *both* CORDIS (the licensee) and MEDTRONIC (the licensor) during the pendency of this Declaratory Judgment action, without unfairly benefitting either.

CORDIS must continue to make the required royalty payments into the escrow. If CORDIS is unsuccessful in its challenge, MEDTRONIC is assured of promptly receiving the escrowed royalties. On the other hand, if CORDIS is successful in its challenge, the escrowed royalties will be promptly refunded. Neither party is given an unfair advantage over the other, and the only detriment whatsoever to MEDTRONIC is the delay in receiving the escrowed royalties. The delay, however, is clearly compensable through the interest earned by the escrow.

Such an escrow arrangement clearly eliminates the "chilling effect" imposed on the challenger-licensee because of the uncertainty about repayment of royalties. As noted earlier, that uncertainty arises, in part, because of the Sixth Circuit's decision in *Troxel* (I) precluding the return of paid royalties. More importantly, this Court and a majority of the Circuit Courts, have *not* decided whether a licensee who is successful in establishing invalidity of the licensed patent is entitled to a refund of paid or escrowed royalties, or whether such royalties are irretrievably lost. Although the Appellate Court held that *Troxel* (I) did not preclude return of royalties, *it expressly refused to decide whether a licensee was entitled to a refund of royalties paid pendente lite.* Under the Federal Circuit decision, the "chilling effect" remains.

The escrow also achieves the objectives of *Lear* by providing an incentive for prompt and vigorous prosecution of the invalidity challenge and a disincentive for delay and dilatory tactics by either party. CORDIS must still make the required royalty payments into the escrow and, accordingly, it is to CORDIS' benefit to prosecute its Declaratory Judgment action vigorously so as to obtain an early refund of the escrowed royalties. On the other hand, because the royalties are not being paid to MEDTRONIC, MEDTRONIC has the same incentive to aggressively pursue a prompt resolution of the issues in order to obtain the escrowed royalties. In contrast, if

the royalties were paid directly to MEDTRONIC, there would be a substantial economic incentive, just as there would have been for the patentee in *Lear*, "to devise every conceivable dilatory tactic in an effort to postpone the day of final judicial reckoning," 395 U.S. at 673.

III. *LEAR* HAS BEEN SUBJECT TO CONFLICTING INTERPRETATION

It is clear that this Court in *Lear* set forth a public policy mandate which reaches far beyond the particular issues and facts in *Lear*. In the seventeen years since *Lear*, however, the lower courts have been without Supreme Court guidance as to the proper scope and interpretation of *Lear*. This has resulted in dramatically inconsistent decisions concerning the application of *Lear* to issues and factual situations not specifically addressed in *Lear*.

It is undisputed, for example, that *Lear* did not specifically address the use of an escrow for post-challenge royalties or the issue of entitlement to post-challenge royalties. However, the actual holding in *Lear* and its public policy mandate plainly have implications that bear directly on these questions, which are raised in the present case. Nonetheless, these issues have been answered, as the District Court acknowledged, in different and conflicting ways by the various Circuit and District Courts.

1. The Sixth And Seventh Circuits Have Endorsed The Escrowing Of Royalties

In *Atlas Chemical Industries, Inc. v. Moraine Products*, 509 F.2d 1 (6th Cir. 1974) and *Precision Shooting Equip. Co. v. Allen*, 646 F.2d 313 (7th Cir. 1981),[5] the Sixth and Seventh Circuit Courts of Appeal endorsed the use of an escrow as the fairest way of managing royalties accruing *pendente lite*, in

[5] A similar analysis and conclusion was reached in *Lee v. Lee Custom Engineering, Inc.*, 476 F.Supp. 361 (E.D. Wis. 1979).

accordance with the principles set forth in *Lear*, as it gives neither party undue burden or benefit.

In *Atlas Chemical*, the Sixth Circuit was reviewing a judgment holding the licensed patent invalid and directing that royalties which had been escrowed *pendente lite* be paid over to the licensor. 509 F.2d at 2. The Court of Appeals affirmed the finding of invalidity, but reversed as to the escrowed royalties. The Sixth Circuit reasoned that payment of the escrowed royalties to the licensor was inconsistent with one of the primary goals of *Lear* — to "unmuzzle" licensees so that an early adjudication of invalidity could be achieved to the real benefit of the public.

According to the Sixth Circuit in *Atlas Chemical*, the existence of an escrow would not change the results insofar as entitlement to post-challenge royalties is concerned, but an escrow would fairly preserve the *status quo:*

> The payment of royalties in escrow does not change the result in this case. *While an escrow is a commendable procedure to preserve the status quo during the course of litigation*, the funds belong to neither party until the validity of the patent is determined. (Emphasis added) 509 F.2d at 7.

The Seventh Circuit Court of Appeals also endorsed the use of an escrow for post-challenge royalties in *Precision Shooting Equipment Co. v. Allen*, 646 F.2d 313 (7th Cir. 1981). That case, like the present case, was an appeal from an interlocutory order establishing an escrow and preliminarily enjoining the patentee from terminating the license.

After a detailed analysis of *Lear*, the Seventh Circuit held that a patent licensee is entitled to a refund of escrowed royalties paid during its patent validity challenge, and particularly approved the use of an escrow to implement that approach—

> [A]ll the post-challenge royalties are safely in escrow for whomever may be found to be entitled to them. It appears

> delay in resolution of the controversy favors neither party. Nor is either party made to assume risks not necessary to the resolution of validity. We adopt that approach. *Id.* at 321.

In summary, the Sixth and Seventh Circuits have both adopted the so-called "challenge approach," which entitles the licensee to a return of any escrowed royalties paid after it has initiated a patent validity challenge — and endorsed the use of an escrow for post-challenge royalties as the most efficient, effective, and fair procedure for achieving the overriding policy considerations of *Lear*.

2. The Second And Eighth Circuits Have, Contrary To The Rationale Of *Lear*, Refused To Allow Escrowing Of Royalties

In *Warner-Jenkinson Co. v. Allied Chemical Corp.*, 567 F.2d 184 (2d Cir. 1977), the licensee brought a suit for declaratory judgment of patent invalidity and sought an order allowing it to deposit royalty payments into escrow *pendente lite*. The District Court dismissed the Complaint because of the existence of the license.

The Second Circuit reversed the dismissal of the complaint and rejected the escrow approach on the ground that it would put undeserved pressure on the licensor. Providing payment directly to the licensor during the challenge, with the possibility of royalty repayment, was in the Second Circuit's opinion most consistent with the statutory presumption of patent validity.[6]

The Eighth Circuit also has refused to allow the use of an escrow for a licensee's post-challenge royalties, *Nebraska Engineering Corp. v. Shivvers*, 557 F.2d 1257 (8th Cir. 1977). That case also involved a declaratory judgment action by a licensee seeking to invalidate the licensed patent. Simultaneously with

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[6] In this case, CORDIS presented evidence which, as acknowledged by the Federal Circuit, arguably rendered the licensed patents invalid.

the complaint, the licensee filed a motion for an order authorizing the licensee to pay royalties to an escrow agent and enjoining the licensor from terminating the license agreement.

The District Court granted the licensee's motion, but the Eighth Circuit reversed, applying a very limited interpretation of *Lear*, and deferring to the Second Circuit decision in *Warner-Jenkinson*.[7] The Eighth Circuit was of the opinion that *Lear* merely prevented *affirmative* enforcement of royalty payment provisions during a licensee's validity challenge. Whether the Court's ruling served or disserved the policy ends of *Lear* was not apparently raised (it was certainly not addressed) in the appeal.

CONCLUSION

The Federal Circuit's decision in this case is contrary, in rationale and effect, to the Supreme Court's mandate in *Lear*. The Federal Circuit's decision that *Lear* should be strictly interpreted will largely undo what *Lear* sought to achieve. It will, on the one hand, create substantial disincentives for licensees to challenge validity; and, on the other hand, create incentives for dilatory trial practices.

There has been no Supreme Court guidance since *Lear* and this has resulted in strikingly different interpretations and applications of *Lear* by the Federal Circuit and District Circuits, particularly with respect to the issues raised in this Petition.

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[7] The Eighth Circuit specifically declined, as did the Federal Circuit in this case, to rule on which party is entitled to royalties paid during the validity challenge.

For the reasons set forth above, it is respectfully requested that this Petition for a Writ of Certiorari be granted.

Respectfully submitted,

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Certificate Of Service

It is hereby certified that at least three copies of the foregoing PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT have been mailed first-class postage prepaid, to:

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Mary W. McGowan

APPENDIX

United States Court of Appeals
for the Federal Circuit

CORDIS CORPORATION,

Appellee,

v. Appeal No. 85-1987

MEDTRONIC, INC.,

Appellant.

DECIDED: December 17, 1985

Before KASHIWA, *Circuit Judge*, SKELTON, *Senior Circuit Judge*, and BISSELL, *Circuit Judge*.

BISSELL, *Circuit Judge*.

This appeal is from the Order of the District Court for the Southern District of Florida, No. 84-2479-CIV-Atkins, (January 10, 1985), granting the motion for relief *pendente lite* of Cordis Corporation (Cordis):

(a) permitting Cordis to deposit into an escrow account all future royalty payments due Medtronic, Inc. (Medtronic) pursuant to the license agreement between the parties; and

(b) enjoining Medtronic from terminating the license agreement because of Cordis' failure to make royalty payments pursuant to the agreement. This in effect protects Cordis from patent infringement or breach of contract counterclaims.

The issuance of the Order by the district court is vacated. The motion for relief *pendente lite* is remanded for further consideration not inconsistent with this opinion.

I

Cordis filed suit against Medtronic seeking a declaratory judgment that the two licensed Medtronic patents, U.S. Patent Nos. 3,902,501 ('501) and 3,939,843 ('843), are invalid (Count I of the Complaint) and that the license agreement between Cordis and Medtronic "is void in its inception" (Count II of the Complaint). Contemporaneous with filing of the declaratory judgment action, Cordis moved for an order to establish a court escrow account into which the royalty payments due Medtronic, *pendente lite*, would be deposited. Additionally, Cordis sought a preliminary injunction to enjoin Medtronic from terminating the license agreement during the pendency of the patent invalidity suit.

The district court, relying on *Precision Shooting Equipment Co. v. Allen*, 646 F.2d 313, 210 USPQ 184 (7th Cir.), *cert. denied*, 454 U.S. 964 (1981), and *Atlas Chemical Industries, Inc. v. Moraine Products*, 509 F.2d 1, 184 USPQ 281 (6th Cir. 1974), granted the motion and permitted Cordis to deposit any royalty payments due Medtronic *pendente lite* into an interest bearing escrow account, with all funds accumulated in the escrow account to be paid to the prevailing party. The district court enjoined Medtronic from terminating the license agreement during the pendency of the action.

Consequently, the issue on appeal to this court is whether the district court properly granted the preliminary injunction and Cordis' motion for establishment of the escrow account.

II

Our jurisdiction over this appeal arises under 28 U.S.C. § 1292(a)(1) and (c) which permits interlocutory appeals from trial court orders granting injunctions. Because a portion of the district court's interlocutory order enjoins Medtronic from terminating the license agreement, we have jurisdiction

over the whole order, including the portion establishing a court escrow account for depositing royalty payments. *Jaffee v. United States*, 592 F.2d 712 (3d Cir. 1979), *on remand*, 468 F. Supp. 632 (D.N.J. 1979), *cert. denied*, 441 U.S. 961 (1979), *aff'd*, 663 F.2d 1226 (3rd Cir. 1981), *cert. denied*, 456 U.S. 972 (1982); *see also United States v. Connolly*, 716 F.2d 882, 885 (Fed. Cir. 1983) (Under 28 U.S.C. § 1292(d)(2), this court's scope of review is not limited to the certified question. We can consider all questions material to the correctness of the interlocutory order.)

III

The Supreme Court, in *Lear, Inc. v. Adkins*, 395 U.S. 653, 671, 162 USPQ 1, 8 (1969), held that a licensee to a patent license agreement is not estopped from contesting the validity of the patent subject to the agreement. *Lear* further held that licensees cannot be required to continue to pay royalties during the time they are challenging patent validity in the courts. *Id.* at 673, 162 USPQ at 9. In *C. R. Bard, Inc. v. Schwartz*, 716 F.2d 874, 219 USPQ 197 (Fed. Cir. 1983), this court held that a patent licensee may seek a federal declaratory judgment to declare a patent, subject to a license, invalid without prior termination of the license.

It is well settled that the purpose of an interlocutory injunction is to preserve the status quo and to protect the respective rights of the parties pending a determination on the merits. *Atlas Powder Co. v. Ireco Chemicals*, 773 F.2d 1230, 227 USPQ 289 (Fed. Cir. 1985); *Smith International, Inc. v. Hughes Tool Co.*, 718 F.2d 1573, 219 USPQ 686 (Fed. Cir.), *cert. denied*, 464 U.S. 996, 220 USPQ 385 (1983); *accord Cate v. Oldham*, 707 F.2d 1176 (11th Cir. 1983). The status of these parties before the district court is that of a patentee-licensor of two patents, each presumptively valid pursuant to 35 U.S.C. § 282, and that of a licensee of those patents.

This court exercises a very narrow scope of review over the district court's grant of injunctive relief. *Smith International,* 718 F.2d at 1579, 219 USPQ at 691. The district court's determination can be overturned only upon a showing that it abused its discretion, committed an error of law, or seriously misjudged the evidence. *Rogers v. Hill,* 289 U.S. 582, 587 (1933); *National File Ins. Co. v. Thompson,* 281 U.S. 331, 338 (1930); *Meccano, Ltd. v. John Wanamaker,* 253 U.S. 136, 141 (1920); *Smith International,* 718 F.2d at 1579, 219 USPQ at 691.

In determining whether to grant or deny the requested injunction, a court must exercise sound discretion and examine the appropriate factors in granting the motion. The factors to be considered in granting a preliminary injunction in the Federal Circuit are the same as those of the Eleventh Circuit. The district court must examine and balance the parties' asserted rights, the acts sought to be enjoined, the likelihood that the movant will prevail on the merits, the irreparable nature of the harm if the injunction is not granted, and whether the public interest is better served by issuing rather than denying the injunction. *Smith International,* 718 F.2d at 1579, 219 USPQ at 690-91; *S J. Stile Associates, Ltd. v. Snyder,* 646 F.2d 522, 525 (CCPA 1981); *accord Cate v. Oldham,* 707 F.2d 1176 (11th Cir. 1983); *Harris Corp. v. National Iranian Radio and Television,* 691 F.2d 1344 (11th Cir. 1982); *see generally Atlas Powder Co.,* 773 F.2d at 1232-34, 227 USPQ 291-93; *Roper Corp. v. Litton Systems, Inc.,* 757 F.2d 1266, 225 USPQ 345 (Fed. Cir. 1985).

We find that several errors of law and a misjudgment of evidence occurred when the district court considered the preliminary injuction factors. Initially, the district court erred in ruling that the *Lear* decision is implicit authority for permitting a licensee to deposit royalties due *pendente lite* into an escrow account pending a determination on the merits. A second error of law appears in the district court's reading that the Sixth

Circuit *Troxel (I)*[1] opinion is authority for the proposition that a licensee may never recoup royalties. Finally, it was a misjudgment of evidence to use evidence to patent invalidity to establish the movant's likelihood of success on the claim that the license "is void in its inception."

Turning to the error committed in reading the *Lear* opinion, we find no authority in *Lear* for establishing an escrow account for royalties due *pendente lite* or preliminarily enjoining a licensor from cancelling the license agreement and, thus, from counterclaiming for patent infringement when this material breach of the license occurs.

Cordis argued and the district court agreed that the Supreme Court decision in *Lear* encouraging vigorous and prompt litigation of invalid patents supports the entry of the requested interlocutory relief. In *Lear*, the Court examined the interests of the licensor, the licensee, and the general public in light of the federal patent policy encouraging prompt adjudication of patent validity, stating:

> Surely the equities of the licensor do not weigh very heavily when they are balanced against the important public interest in permitting full and free competition in the use of ideas which are in reality a part of the public domain. Licensees may often be the only individuals with enough economic incentive to challenge the patentability of an inventor's discovery. If they are muzzled, the public may continually be required to pay tribute to would-be monopolists without need or justification. We think it plain that the technical requirements of contract doctrine must give way before the demands of the public interest in the typical situation involving the negotiation of a license after a patent has issued.

Lear, 395 U.S. at 670-71, 162 USPQ at 8.

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[1] *Troxel Manufacturing Co. v. Schwinn Bicycle Co.*, 465 F.2d 1253, 175 USPQ 65 (6th Cir. 1972) (*Troxel I*).

This public policy statement *does* permit a licensee to cease payments due under a contract while challenging the validity of a patent. . It *does not* permit the licensees to avoid facing the consequences that such an action would bring. The holding of *Lear* only prevents the affirmative enforcement by the licensor of the royalty payment provisions of the license agreement while the patent's validity is being challenged by the licensee.

We believe that the reasoning succinctly stated by the Second Circuit in *Warner-Jenkinson Co. v. Allied Chemical Corp.*, 567 F.2d 184, 193 USPQ 753 (2d Cir. 1977) and followed by the Eighth Circuit in *Nebraska Engineering Corp. v. Shivvers*, 557 F.2d 1257, 195 USPQ 227 (8th Cir. 1977) is in keeping with the holding of and policy statements in *Lear:*

> We believe that if the plaintiffs wish to continue to invoke the protections of their licensing agreements, they should be required to continue paying their royalties to the defendant. Ultimately, all royalties paid after the filing of the complaint *may* have to be returned to the plaintiffs. . . . At present, plaintiffs already have the option of withholding royalties and thereby breaching the licensing agreement; of course, they would then run the risk of an injunction if they should lose on the merits. It would not be fair for the plaintiffs to be allowed simultaneously to reap all the benefits of the licensing agreement and to deprive the licensor of all his royalties. Patents are presumed to be valid, 35 U.S.C. § 282; until invalidity is proven, the patentee should ordinarily be permitted to enjoy the fruits of his invention. The principal effect of an escrow arrangement would be to put undeserved pressure on the defendant.

Warner-Jenkinson, 567 F.2d at 188, 193 USPQ at 753 (emphasis added).

In addition to the misapplication of *Lear* in evaluating the rights and obligations of the parties and the interest of the public, the district court made errors of law in determining whether irreparable harm would occur to the licensee if the preliminary injunction was not granted.

To support its request for injunctive relief, Cordis argued that absent such relief it would experience irreparable harm in one of the following four ways: (1) being exposed to a potential patent infringement suit, (2) risking forfeiture of royalties paid while litigating the validity of the patents,[2], (3) foregoing contesting the validity of the patents, or (4) terminating any manufacture, use or sale of the tined leads covered by the '501 and '843 patents.

Cordis argued to the district court that any one of these alternatives, when balanced against the harm suffered by Medtronic in receiving delayed royalty payments, tips the scales of equity in favor of permitting royalties due *pendente lite* to be deposited into an interest bearing escrow account.

With regard to Cordis' first, third, and fourth assertions of irreparable harm, for the reasons stated above, *Lear* provides no reprieve. Moreover, Cordis made no showing that Medtronic is financially irresponsible or might be judgment-proof at the end of the litigation. "Only a viable threat of serious harm which cannot be undone authorizes exercise of a court's equitable power to enjoin before the merits are fully determined. (Citation omitted). A preliminary injunction will not issue simply to prevent a mere possibility of injury, even where prospective injury is great." *S. J. Stile*, 646 F.2d at 525; *See Smith International*, 718 F.2d at 1579, 219 USPQ at 692.

With regard to Cordis' second assertion of irreparable harm, the district court's reliance on *Troxel (I)* is misplaced. Neither the *Troxel (I)* nor *Troxel (II)* decisions by the Sixth Circuit prohibit the licensee from recouping royalties paid *pendente lite* once the patent subject to the license agreement is proved invalid. The *Troxel* decisions only prohibit the licensee from recovering and retaining royalties paid or due prior to the

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[2] Cordis cites the *Troxel I* decision and the subsequent *Troxel Manufacturing Co. v. Schwinn Bicycle Co.*, 489 F.2d 968, 180 USPQ 290 (6th Cir. 1973), *cert. denied*, 416 U.S. 939, 181 USPQ 417 (1974)(Troxel II), decision as authority for this position.

adjudication of invalidity when the challenge to the patent was made by a third party. Since the district court improperly evaluated the rights of the parties and the interest of the general public under *Lear*, we need not address the risk of forfeiture question any further than the district court's application of *Troxel (I)*. Nor do we decide which party is entitled to royalties paid or accrued *pendente lite*.

Finally, the district court erred in evaluating the likelihood of success factor. To show likelihood of success on the merits, Cordis offered only the affidavit of an engineer employed by Medtronic's competitor, Pacesetter, which set forth that Pacesetter publicly disclosed and/or developed certain devices covered by claims of the patents in suit prior to Medtronic's alleged date of invention. The district court's error occurred in using evidence of patent invalidity to establish the movant's likelihood of success on the claim that the license "is void in its inception" (Count II). The affidavit by an employee of Medtronic's competitor setting forth facts is arguably sufficient to prove that the patents in suit are invalid under the provisions of 35 U.S.C. § 102(a) and (b). However, this affidavit alone is insufficient to support the movant's likelihood of success on the second count of the complaint, that is, that the license agreement "is void in its inception." Patents are issued by the government after examination and evaluation of the patent application by the United States Patent and Trademark Office and are presumed valid once issued. 28 U.S.C. § 282. As observed by the Sixth Circuit, "Congress has not seen fit to create an implied warranty of validity in license agreements." *Troxel (I)*, 465 F.2d at 1260, 175 USPQ at 70. "Absent fraud or misconduct, a patentee should not be held responsible for the issuance of an invalid patent." *Id.* at 1259, 175 USPQ at 69.

Consequently, because the analysis underlying the district court's order is erroneous, the order is vacated and the motion remanded for further consideration not inconsistent with this opinion.

VACATED AND REMANDED

United States Court of Appeals
for the Federal Circuit

CORDIS CORPORATION,
Appellee,

v.

MEDTRONIC, INC.,
Appellant.

No. 85-1987

ORDER

A petition for rehearing and a suggestion for rehearing in banc having been filed in this case,

UPON CONSIDERATION THEREOF, it is Ordered by the court that the petition for rehearing be, and the same is hereby, Denied.

The suggestion for rehearing in banc is declined.

FOR THE COURT

/s/ FRANCIS X. GINDHART
Francis X. Gindhart, Clerk

Date: February 14, 1986

cc: Lawrence C. Brown
Granger Cook, Jr.

United States District Court
Southern District of Florida

Cordis Corporation,

Plaintiff,

v.

No. 84-2479-
CIV-Atkins

Medtronic, Inc.,

Defendant.

Order GRANTING Cordis' Motion For Establishment Of Escrow Fund And For Preliminary Injunction

This cause is before the court on plaintiff, Cordis Corporation's Motion For Establishment Of Escrow Fund And For Preliminary Injunction. Based upon careful consideration of the record and oral arguments in this case, it is hereby

ORDERED AND ADJUDGED that the Motion is GRANTED.

Until final judgment is rendered in this action, Cordis will be permitted to deposit any royalty payments due and owing to Medtronic, Inc. into an interest-bearing escrow account, provided that upon final judgment, all funds accumulated in the escrow account are to be paid over to the prevailing party, and Medtronic, Inc. is enjoined from terminating the License Agreement during the pendency of this action.

The court notes that the circuits are split on the issue of whether to establish escrow accounts for the collection of royalty payments during the pendency of patent infringement suits. I have decided, however, that *Precision Shooting Equipment Co. v. Allen*, 646 F.2d 313 (7th Cir. 1981) and *Atlas Chemical Industries, Inc. v. Moraine Products*, 509 F.2d 1 (6th Cir. 1974) are more faithful to the spirit of *Lear, Inc. v. Adkins*, 395 U.S. 653 (1969), where the Supreme Court held that licensee estoppel is no longer valid law.

Under well-established case law, the party requesting a preliminary injunction bears the burden of establishing to the District Court that: 1) It has a substantial likelihood of eventual success on the merits; 2) Irreparable injury will be suffered unless the injunction issues; 3) The threatened injury to the movant outweighs the damage which the injunction may cause the opponent; and 4) The injunction would not be adverse to the public interest. *Productos Carnic, S.A. v. Central American Beef and Seafood Trading Co.*, 621 F.2d 683, 685 (5th Cir. 1980); *Dallas Cowboy Cheerleaders, Inc. v. Scoreboard Posters, Inc.*, 600 F.2d 1184, 1187 (5th Cir. 1979); *Texas v. Seatrain International, S.A.*, 518 F.2d 175, 179 (5th Cir. 1975). The Affidavit of Harry W. Fletcher sets forth the fact that PACESETTER publicly disclosed and/or developed certain devices covered by the claims of U.S. Patent No. 3,902,501 prior to the alleged invention defined by the claims of such patent. If this allegation is proven true, than the patents-in-suit would arguably be invalid under the provisions of 35 U.S.C. 102(a) and (b). Second, if Cordis fails to make its royalty payments to Medtronic, it will be vulnerable to a patent infringement action, with the prospect of paying treble damages and of being enjoined from manufacture and sale of the licensed products. If Cordis continues to make royalty payments while seeking to invalidate the patents in suit in this action, the royalty payments made to Medtronic cannot be recovered under *Troxel Manufacturing Co. v. Schwinn Bicycle*, 465 F.2d 1253 (6th Cir. 1972). Once the royalty payments are made, there is no legal remedy available for repayment. If there is no legal redress, Cordis would be irreparable damaged. This damage far outweighs any damage Medtronic would suffer by the issuance of an injunction preventing the termination of the license agreement and the establishment of an escrow account for payment of royalties. Finally, the public has a clearly established interest in having invalid patents challenged in Federal courts. Should Cordis be successful, the claimed subject matter of the patents at suit would enter the

public domain and Medtronic would no longer be entitled to maintain a legal monopoly in the claimed subject matter. The public interest would clearly be served by providing Cordis with reasonable protection so that it may challenge two patents which it believes invalid.

Done and Ordered at Miami, Florida this 10 day of January, 1985.

/s/ CLYDE ATKINS
CLYDE ATKINS
United States District Judge

CC: Lowell L. Garrett
Granger Cook, Jr.
George H. Gerstman
Henry W. Collins
Hal Vogel